A GUIDE TO

HIGHER ED PUBLIC-PRIVATE PARTNERSHIPS

BRAILSFORD & DUNLAVEY

WHAT IS THE HIGHER ED P3 GUIDE?

Brailsford & Dunlavey presents a seven-part series on public-private partnerships ("P3s") in the higher education space, intended to educate readers on this dynamic market—its history, opportunities, misconceptions, and more. It should be noted that every P3 deal is unique and this document is only an introductory overview.

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Part 1

INTRODUCTION

Colleges and universities are facing limited resources—a reality we are all aware of. In response, schools are looking at all of their services and evaluating what is critical and core to their academic mission. With priorities in mind, they're then looking for creative ways to make needed projects happen. As a result, every year many schools partner with private sector parties (e.g., developers) under the notion that the whole is greater than the sum of its parts—that, together, these partners can do more, and do it efficiently and effectively. And when it comes to repairing or improving the country's aging campuses and their facilities, there are a lot of opportunities for partnership—including facilities' design, construction, financing, and long-term operation and maintenance.

What is a P3 and what does one look like?

That's a surprisingly tricky question. At the moment, there is **no common definition** of a P3, there is no centralized governing body overseeing P3s, and there is a limited breadth of experience in the higher education sector in the US. So in the simplest terms, a higher education P3 is a development/deal structure in which a public or private college or university takes on a private sector partner (or partners) to share in the resources, risks, and incentives that come with the development and operation/maintenance of campus facilities. The National Council of Public-Private Partnerships identifies **18 different legal and financial P3 structures**, and each P3 agreement is unique to the partnership, or deal.

P3s are not a silver bullet. They are not short-term engagements, nor are they without their challenges; indeed many in the P3 world think of them as marriages. They are simply **one type of alternative delivery method for schools to finance projects** that might otherwise go unfinanced, to leverage assets like land, to transfer risk, and to ensure operational success for years to come.

Colleges and universities look to P3s for many reasons, but most often because **funding is a challenge**. With aging campuses, and given the idea that new facilities can be important differentiators, schools are looking for **creative ways to continue improving the student experience**—even in the face of debt financing/capacity limitations. Beyond offering a vehicle for financing, P3s can also allow for development and operational risk transfer. Specifically, P3s can be structured to leverage expertise, avoid potential institutional procurement challenges, improve operational efficiencies, and more. In short, if a university is at Point A and wants to get to Point B, P3s are one way to bridge the distance.

Despite the term "*public*-private partnerships," higher ed P3s can happen at private institutions. While current research shows that the most common institutional profile for a P3 project in higher ed is a large public university, private institutions have begun utilizing partnerships more frequently. Likewise while P3s in higher education initially were sought after only for housing projects, now the engagements apply to a range of campus assets, including mixed-use featuring retail, student unions, campus recreation, hotel and conference centers, campus edge, health & wellness centers, office buildings, research parks, dining facilities, hospitals, and workforce/faculty/staff housing, among others.

As deal structures, **P3s are incredibly complex.** Each one is different, and each is almost unwieldy due to its many moving parts and parties. The stakes are also high because P3s are true partnerships—as a university, you're not picking a one-time collaborator for a quick job, you're picking **a partner who you'll work with for potentially the next several decades**… who your successors will need to successfully work with, and who will work hard to improve your students' experience for years and years to come.

P3s get a lot of press these days, with some people praising them and others demonizing them. Indeed, each claim can feel justified depending on how you look at P3s as a concept and which case studies you consider. But **P3s are not black and white.** They are potentially a world of opportunity, resources, creativity, and collaboration… and at the same time, potentially a world of misrepresentation, control issues, and difficult relationships. So here's the interesting part: Which world you end up in is up to you and your specific project. This is not about chance or luck, because P3s absolutely can be designed to ensure success. It just takes a whole lot of education, thoughtful planning, and vision. And, as needed, the wisdom to walk away.

Part 2

A BRIEF HISTORY

The P3 development model first emerged as a formal business relationship between a college or university and private developer/operator in the U.S. in the 1960s. Early on, the institution typically provided the land and the developer/operator designed, constructed, financed, owned, and/or managed the asset. Schools were at a big disadvantage here—due to lack of sophistication (or industry understanding)—and those without an advisor or way to educate themselves were typically negotiating with developers with a lot more experience.

The model evolved in the 1990s.

This is when tax-exempt financing became an obtainable funding source for development firms. Schools saw an opportunity to leverage their limited resources and carry out capital projects without tapping into their debt capacities. They also began learning how to navigate the world of P3s.

As recently as the late 1990s, P3s in higher education existed in only seven states. **Between 1997 and 2015, the number of transactions exploded,** and by the end of that period, transactions had been completed in over 35 states with approximately $13 billion worth of bond issuances for P3s. Over the last few years, P3s in higher ed have started to include more mixed-use components.

At the same time, **additional large players have entered the development space,** driving down capitalization rates as student housing and mixed-use projects have become a desirable asset class. Some of the most notable mixed-use P3 projects include developments at Drexel University, The University of South Florida, The Ohio State University, University of Kentucky, Texas A&M University, Houston Baptist University, Louisiana State University, Rowan University, and Seattle University, just to name a few.

When a developer equity model emerged with student housing developers obtaining access to equity capital, **some developers shifted from a fee approach to an ownership model.** Limited comprehensive data is currently available for equity-based transactions but large equity-based development deals have been realized at Arizona State University, Rochester Institute of Technology, Trinity College, and Syracuse University, to name a few. Two large student housing Real Estate Investment Trusts (REITs) became publicly listed in 2004 and 2005, and their success has led to legitimizing an industry.[1] It has also marked an arrival of local and regional players in many states that have evolved their off-campus student housing business into more sophisticated partnership projects with surrounding colleges and universities.

Meanwhile capitalization rates have narrowed between student housing and multifamily housing within the last three to four years. Student housing has become a desirable asset class compared to multifamily housing given the stability of the student housing sub-market and the addition of new REIT capital players.

[1]As of June 2018, one of these REITs is under agreement to be purchased.

Part 3

PROS AND CONS

There is no one easy, simple Pro/Con list for P3s. Why? Each university has its own perspective, and some perspectives differ slightly while others differ greatly. Consider that for one school, having control over the operation of a new facility is ideal, while for another school ideal might be turning over operation to a private partner. That means “lack of control over operation” is not necessarily a pro or a con.

Of course, we’ve seen that there are general trends.

As you look over the lists below, consider that they’re not hard and fast rules, but generalities.

Reasons to do a P3

- Developer takes risk of upfront costs, budget, operations, and schedule
- Streamlined procurement
- Commercial construction standards lower development costs
- Leverages developer’s experience as expert in construction
- Sometimes can preserve the debt capacity of institutions with limited borrowing ability
- Guaranteed financial returns to university through ground lease payments or as excess cash flow beyond the required debt coverage ratio
- The private sector partner will be contractually obligated to meet certain performance metrics throughout the agreement
- Could be credit positive
- Can usually accelerate the schedule

Reasons not to do a P3

- University may lose out on important revenue stream
- University may be required to provide guarantee to developer
- University may already have in-house development and/or management expertise
- University can obtain lower cost to capital than a foundation tax-exempt bond financed or private equity financed model
- Additional costs such as legal, development, and financing fees
- Possible negative impact to university’s balance sheet and debt profile
- May increase cost to students
- University might not have procurement concerns

For universities that have decided against a P3, ultimately the “reasons not to do” list spoke louder—or there were deal-breakers that could not be resolved. For universities that have decided to embark on a P3, the “reasons to do” list won out. Which is to say, P3s aren’t all good and they aren’t all bad—they just *are*. They have benefits and they have drawbacks, just like any other delivery structure.

Part 4

DEVELOPMENT STRUCTURES

P3 deals are not solely building and construction deals, but financial and operational risk transfer agreements. How much risk is transferred, and how much control a university retains, varies greatly depending on the type of development structure.

This series gives a sense of what can be expected from each structure type.

Note that there's a big asterisk here, since the structures covered are not exhaustive, and since each P3 deal is different and can be customized to what the involved parties want. As a window into the big picture, let's look at risk transfer. As you move from blue to yellow along the below spectrum, risk is transferred away from the university and to the private sector partner. Notice that who owns, operates, and finances the project changes as you move from a traditional structure (non-P3) to a fully privatized structure.

T	F	C	E	P
TRADITIONAL	**501(c)3 Foundation**	**CONCESSIONAIRE**	**EQUITY**	**FULLY PRIVATIZED**
University owned	501(c)3 owned	University owned	Developer owned	Privately owned
University operated	Operations vary	Privately operated	Privately operated	Privately operated
University financed	Financed through a ground lease	Developer financed	Financed through a ground lease	Privately financed *(University may have leasing agreement)*

A	B
University Affiliated	**National**
University operated	Privately operated

Traditionally, financing is through the institution and the school has the option to implement various delivery methods such as design-bid-build, construction manager at risk, design-build, etc. This is the way most schools have traditionally delivered their capital projects.

On the following pages, the various P3 development structures are explained in more detail.

University or Unaffiliated Foundation

The school ground leases land (typically for 30 to 40 years) to an affiliated or non-affiliated 501(c)3 non-profit foundation that issues the debt to build a project it owns. The foundation then engages a fee developer to design and build the project. Upon completion, the facility is managed by the college or university, a private entity, or some type of shared governance model that has become increasingly common. Ownership of the improvements typically revert back to the university after the retirement of the debt service and expiration of the ground lease.

Generally, the school has the option to terminate the agreement early by purchasing the improvements simply by paying off the debt. In addition, depending on the deal structure, various agreements may be needed to finalize the financing, including potentially a master lease, first fill agreement, university marketing assistance, and/or a non-compete condition—all as applicable to the asset class. Any surplus revenue can be retained by the school for any lawful use. In this type of deal structure, the debt can impact both the school's balance sheet and credit.

Pros

- Typically tax-exempt debt
- Typically no real estate taxes
- University has no financial commitment
- Cost of capital is low-to-moderate
- Some of cash flow goes to the school (waterfall)
- Ground rent
- Could be credit positive for the institution

Cons

- Debt can impact the school's balance sheet
- Debt can negatively impact university's credit
- Additional costs associated with this type of transaction (e.g., capitalized interest, debt service reserve fund, annual fees)

Spotlight: Louisiana State University

By choosing a P3 with a 501(c)3 development structure, LSU accelerated the replacement and renovation of its housing by 5+ years, preserved its debt capacity, retained housing and res life programming authority, and received ground lease payments and surplus cash flow—est. at $218M over the 40-year ground lease.

Equity

A developer purchases or ground leases land (typically 40–80 years) from the institution and privately finances the project. The private partner designs, builds, owns, and usually but not always asset manages the project with varying levels of university involvement depending on the deal. The project reverts to college or university ownership at the end of the ground lease. In addition, depending on the deal structure, various agreements may be needed to finalize the financing including a master lease, any fill agreements, marketing assistance from the school, or a non-compete condition. Ground rent and revenues are negotiable. Depending on various factors, any project-related debt can be treated off the school's balance sheet and have a low impact to credit, thereby reserving debt capacity for other campus projects.

Pros

- School has no financial commitment (reserved debt capacity)
- Some cash flow goes to school (waterfall)
- Ground rent

Cons

- School has little control of improvements
- Cost of capital is moderate-to-high
- Real estate taxes
- Debt is not tax-exempt

Spotlight: University of South Florida

By choosing a P3 with an equity development structure, USF maximized its financial return while concurrently deferring project delivery, operating, and budget risk to its private partners. The $133M USF Village is opening in two phases (fall of 2017 and fall of 2018) and will feature 2,150 beds, campus recreation facilities, dining facilities, and retail space including the first Publix grocery store on a college campus.

Concessionaire

Let's look at this through the lens of student housing. A concessionaire and school enter into a master concession agreement ("MCA") in which the school contributes all or most of its existing housing portfolio. Housing system revenues are pledged to a third-party lockbox. The concessionaire utilizes its administrative rights to the revenues in the lockbox to raise outside capital for investment in the housing portfolio. The capital raised is first used to defease any outstanding debt on existing facilities, with the remainder then allocated to enhance existing projects and implement new projects, and to establish a reserve fund. The MCA is typically a 50+ year agreement that outlines how the assets will be maintained and operated.

In coordination with the college or university, the concessionaire:

- designs and constructs new housing
- renovates/repairs existing facilities
- manages, operates, and maintains the facilities over the life of the concession

The school:

- collects housing fees (which allows for students' use of financial aid for housing)
- is responsible for marketing the assets and room assignments
- manages the student life aspects of the housing program, as well as security

Future revenues cover operating expenses, repair & replacement, operations & maintenance, and capital reserves. The net operating income ("NOI") of the system pays the debt service on the capital raised, and concessionaire fees. After debt service and fees, remaining revenues flow into a facility reinvestment fund, with the remaining portion being contributed back to the institution. As the concessionaire (i.e., not the college or university) holds the note, the agreement is usually treated as balance sheet and credit neutral, though this is not always the case.

Pros

- School has high control of improvements
- School has no financial commitment
- No ground lease (flexibility)
- Cost of capital is low
- Most of cash flow goes to the college or university (waterfall)
- Accelerated delivery schedule due to alternative financing & concessionaire incentive for payment
- Concessionaire is incentivized to optimize lifecycle costs (energy efficiency, etc.) that might have gone unconsidered

Cons

- May incur real estate taxes
- Debt is not tax-exempt
- Large amount of fees
- Would likely include the majority of the school's housing stock

Spotlight: Wayne State University

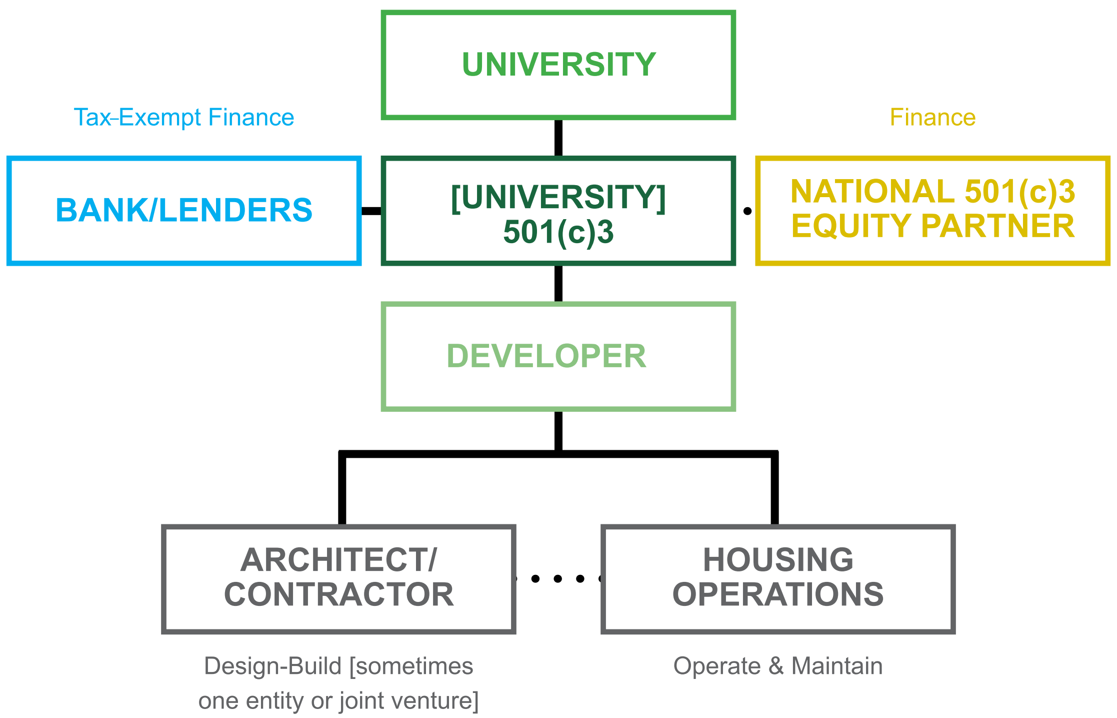
By choosing a P3 with a concessionaire development structure, Wayne State was able to accommodate its students' residential needs without impacting the university's credit. The effort will renew the university's housing program through a combination of new construction, demolition, and strategic renovation of existing facilities.

While the variety of impacts and risks associated with each of the P3 structures may be confusing at first, ultimately it's beneficial to all parties involved that so much variety exists. What works for one college or university does not work for another, and what works for one private partner does not work for another. Being able to choose among the existing structures (including not choosing a P3 at all)—or to blend them—allows each development to best serve the parties involved.

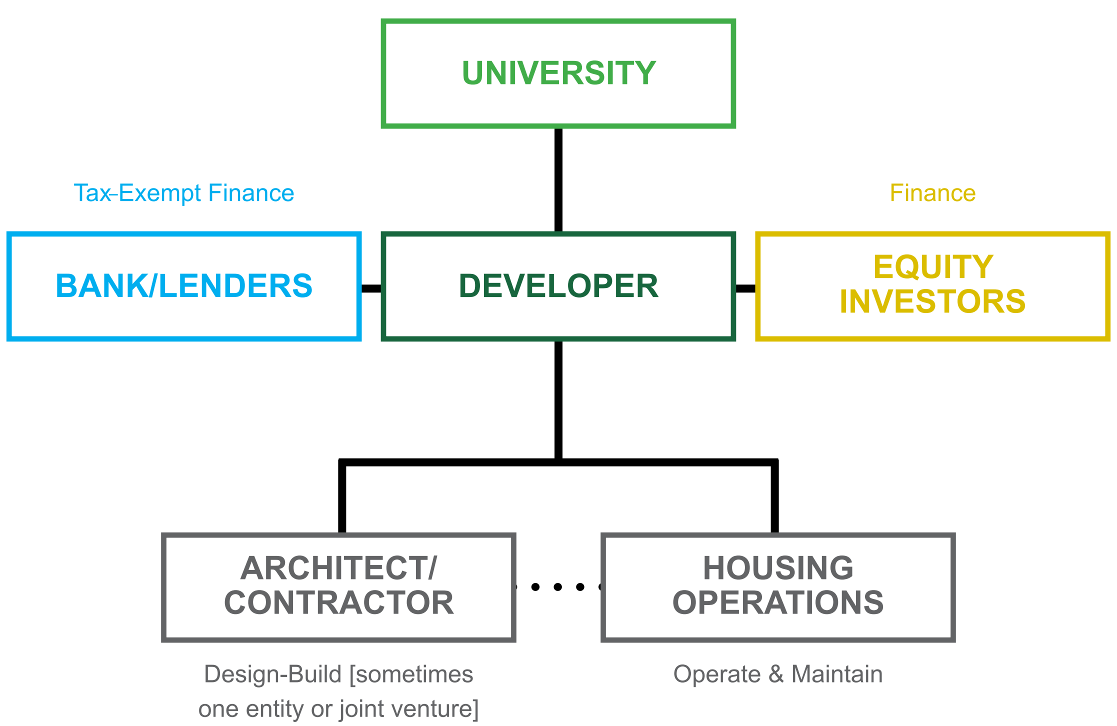
If after reading this guide you believe a P3 is your best option for developing a new asset, rest assured that it is all navigable and that many schools have gone through this process before you.

Here's a look at the University or Unaffiliated Foundation, Equity, and Concessionaire models as organizational charts

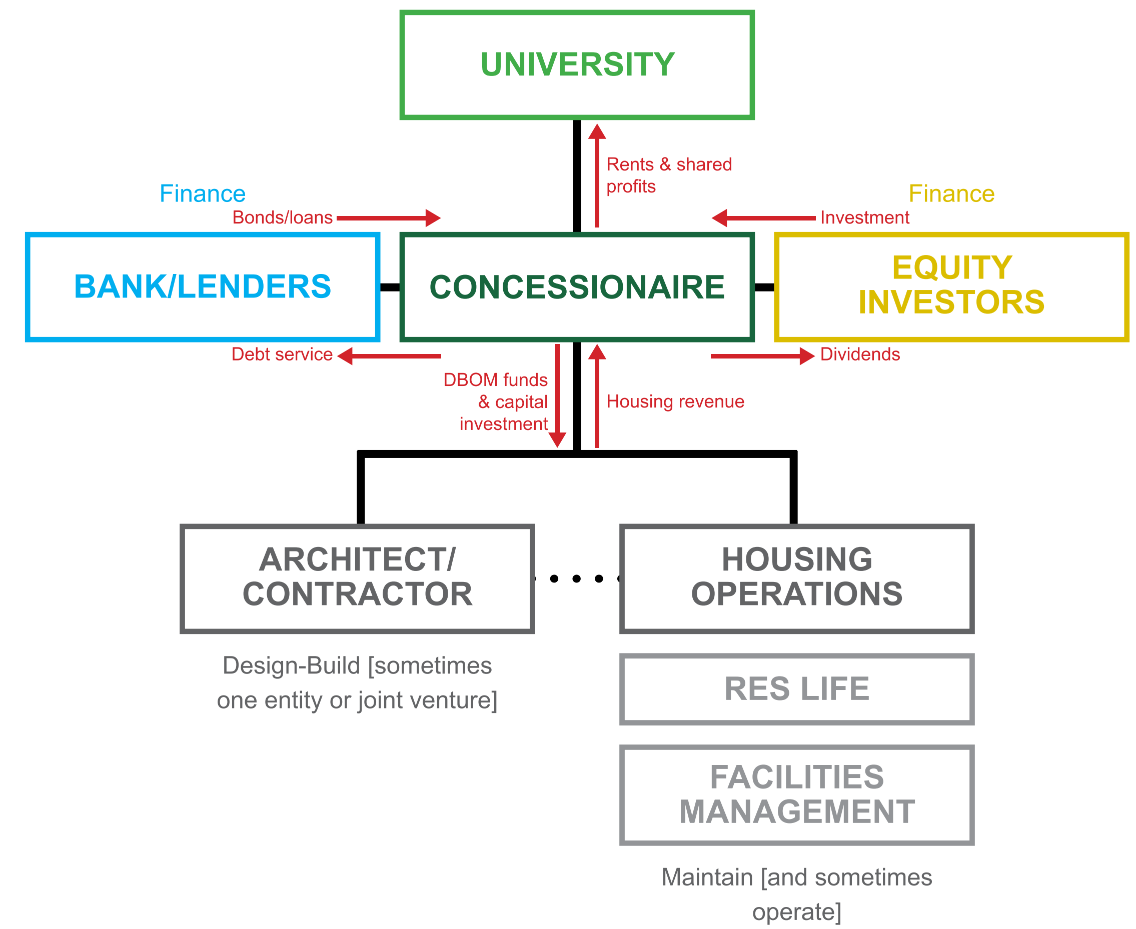
University or Unaffiliated Foundation



Equity



Concessionaire



Part 5

9 ATTRIBUTES OF A GOOD ENGAGEMENT

Although all P3s present higher education institutions with an alternative delivery method, not all P3s are created equal.

The following attributes make a successful relationship much more likely.

1.
Clear definition of expected outcomes

While this is seemingly obvious, we have seen that it is nonetheless common for there to be some disconnect about what the parties expect to achieve through the P3. Ensuring that parties on both sides are on the same page is crucial.

2.
Sufficient development time

P3s are complicated transactions so institutions must allow sufficient time for negotiating the structure and required legal agreements of the project.

3.
A true partnership, not a master/servant relationship

P3s work well when both parties have mutual respect and consideration for each other, and are invested in each other's success.

4.

Honesty

Nothing implodes a P3 faster than a lack of trust among the parties.

5.

A fair and equitable contract/management agreement

Related to the first point, it is crucial that expectations are clearly spelled out in an operating agreement that allows both parties to know exactly what is expected and how success will be measured.

6.

A close working relationship with the institution

For the relationship to work, the private contractor must have support from and access to campus leaders.

7.

Consistency among all properties, whether privatized or university managed

Given that students flow freely back and forth among properties, it is imperative that the facilities be managed and maintained equitably. For schools, that means embracing a *pari passu* mentality—ultimately considering and treating private properties as equals.

8.

Intentional design and construction

The privatized property must be of a quality defined by the institution.

9.

Flexibility

The private contractor should have latitude to shop for the most cost-effective solutions available.

Part 6

COMMON MISCONCEPTIONS

Whether you've heard good or bad things about P3s, chances are you've heard something incorrect.

Here are some misconceptions we come across frequently—and the real story.

1.

Soon every project will be a P3

P3s are the right answers for some projects, but in other cases they're best avoided. While we've seen more and more universities express interest in P3s over the years, P3s will never fully replace traditional models, nor should they. P3s are not always more cost-effective, not always faster, and not always better. They are simply one of many ways to bring a project to fruition, and the more options a university has, the better. We work with a lot of universities—hundreds of them. Some express an interest in P3s, and we go on to recommend a P3 development structure. Others express an interest and we steer—and strongly steer—them away from a P3. P3s are not a silver bullet.

2.

P3s are privatization—or are equivalent to privatization

If a university wants to fully privatize its assets, it can do that. It can fully relinquish ownership over an asset, and the private sector entity can fully own and operate the asset. But that's not a P3. During the period of a P3 (generally 30–80 years depending on the deal structure), the private sector partner has leasing rights to the asset, and can manage it as laid out in the agreement. That's not full ownership, and as a result the private sector partner does not have typical ownership rights like selling or mortgaging the asset.

3.

P3s in higher education can only be used for student housing

While P3s in higher education mostly originated in student housing, the model has successfully been applied to a variety of assets. For example, we've worked on and seen P3 projects for the following asset types: mixed-use featuring retail, campus recreation, hotel and conference centers, campus edge projects, student unions, hospitals, health & wellness facilities, and workforce/faculty/staff housing, among others.

4.

P3s are only for new construction

While much of the P3 work we've seen results in new development, there is a fair amount of modernization and maintenance work that takes place through P3s.

5.

If our university does a P3, we'll have no control over the project

A university can retain as much or as little control as it wants over the development of the asset, depending on the type of P3 development structure selected. Once the asset is built and in operation, the university can retain control either by remaining the operator or, if the private sector partner is the operator, tracking the asset's performance against metrics worked into the P3 agreement. If the private sector partner cannot meet the agreed-upon performance metrics, the university can react.

6.

In a P3, the private sector partner funds the project

The private sector doesn't fund the project, but finances it—a minor difference in language, but a huge difference in reality. The private sector partner can source funds from a variety of areas, including but not limited to traditional debt financing, private equity, and economic development incentives.

7.

The only reason universities pursue P3s is the financing help

Private financing can be a huge draw—that is a definite. Beyond private financing, though, there are many reasons universities look to P3s. They include: risk transfer, faster project delivery, minimization of costs throughout the asset's lifecycle, etc. Remember that a P3 is so much more than just building or renovating an asset; usually it's a multi-decade relationship.

8.

If my university does a P3, my job will be cut

Nothing is a guarantee, of course, but our experience has not shown this to be the case. Often a P3 is even a means for empowerment and professional advancement, as the university will need educated employees to oversee the developer's design, construction, financing, operation, and/or maintenance of the facility.

Part 7

THE VALUE OF AN ADVISOR

In addition to all the usual reasons a university might turn to an advisor—including the inspiration and empowerment necessary to advance university communities—advisors are especially helpful when evaluating and embarking on a P3.

Here are some things you can expect of most any advisor.

They will:

- Help the college or university navigate the various P3 deal structures
- Drive the process of the transaction (through ribbon cutting, if wanted!). Even though each P3 is different, an advisor knows what comes next in the process—what to look for, what to do, and what to avoid
- Serve as the "team captain" or "orchestra conductor," ensuring everyone shows up at the right place at the right time, and works together
- Work alongside the school as it receives legal advice
- Oversee the program, budget, and timeline to ensure a project is delivered on time

Additionally, some advisors offer a higher level of service and all-important impartiality. These advisors can:

- Help define the project and ensure market viability in a way that is consistent with the school's mission
- Act 100% in the school's best interest; these advisors are agnostic as to whether the building gets built or how it's funded
- Ensure an honest and fair RFP/RFQ process (e.g., selection of private sector partner) due to impartiality
- Have relationships with professionals in every aspect of the deal—architects, developers, contractors, etc.—that can be leveraged as best serves the university
- Specialize in higher education, giving them the expertise to enrich the project and fully integrate themselves within the context

ABOUT B&D

Founded in 1993, Brailsford & Dunlavey is a program management and development advisory firm with comprehensive in-house planning capabilities, dedicated to serving educational institutions, public agencies, and non-profit clients. Acting as advisors, we shepherd an idea, make it a viable project, and oversee it through ribbon cutting and into operation. We are nationally recognized as a leader in the higher ed P3 market and were nominated for P3 Bulletin's 2017 Technical Advisor of the Year award.

If you would like more information, please contact Doug Kotlove at dkotlove@programmanagers.com.

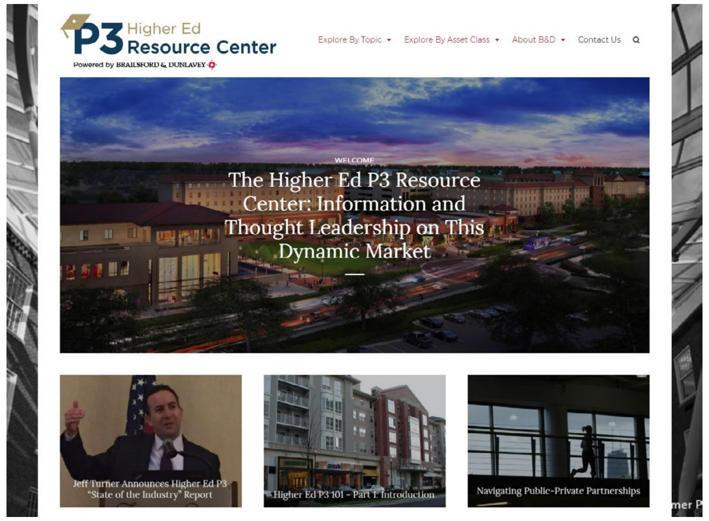
25 years — EST. 1993 — OF INSPIRING, EMPOWERING, AND ADVANCING COMMUNITIES

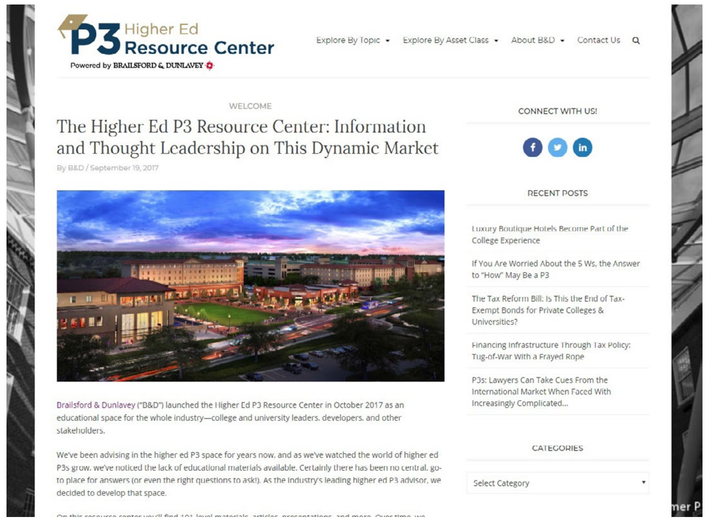
P3 Higher Ed Resource Center

Powered by BRAILSFORD & DUNLAVEY

In 2017, B&D launched the **Higher Ed P3 Resource Center (www.p3resourcecenter.com)** as an educational space for the sector—college and university leaders, developers, and other stakeholders. Serving as a central, go-to place for answers—or even the right questions to ask—the resource center offers articles from industry experts, infographics, presentations, and more.

The Higher Ed P3 Resource Center serves as a library, housing information from throughout the industry. It also includes B&D's annual State of the Industry Report, which gives a detailed account of the year's average project costs, deal structures, ground lease terms, real estate asset class mixes, and other factors.





Pizza
Coffee
TIGER Grille
Coffee
PHONE REPAIR
LOUISIANA SUBS
SUPER CUTS
Ice Cream
RESTAURANT
LSU

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